SA institutional investors to adapt to new playing fields

South Africa's institutional investors have been challenged to conduct their business on a new playing field following publication of the Draft Code for Responsible Investing.

David Geral, a partner at corporate law firm Bowman Gilfillan, alerted delegates to a recent seminar in Johannesburg of the Code's main principles:

- Institutional investors should incorporate environmental, social and governance (ESG) considerations into their investment analysis and activities as part of the delivery of superior risk-adjusted returns to the ultimate beneficiaries;
- Institutional investors should demonstrate their ownership approach in their investment arrangements and activities;
- Where appropriate, institutional investors should consider a collaborative approach to promote acceptance and implementation of the Code's principles, and those of other codes and standards applicable to institutional shareholders; and
- Institutional investors should be transparent about their policies, how they are implemented and how the Code is applied to enable stakeholders to make informed assessments.

"The common law and statutes impose a duty on some institutional investors, such as pension funds, to act at all times in the best interests of the person to whom the duty is owed," said Geral. "And that duty must be applied to the exclusion of all competing interests."

He stressed that the duty is owed to the fund, its members and beneficiaries.

Geral said that the Code builds on those "best-interests-of-members" requirements in the Pension Funds Act, that hint at proper decision making and risk management processes, rather than specific outcomes.
Geral referred to a 1984 English case, *Cowan and others v Scargill and others*, as especially instructive in pointing to the best interests of the beneficiaries.

"When the purpose of the trust is to provide financial benefits for the beneficiaries, as is *usually* the case, the best interests of the beneficiaries are *normally* their best financial interests."

And when it came to the power of investment, that power had to be exercised so as to yield the best return for the beneficiaries judged in relation to the risks of the investments in question.

Geral said that "benefit" was a word with wide meaning. The court acknowledged that arrangements which work to the financial disadvantage of a beneficiary may yet be for his benefit. Hence, benefit *can* be other than pure financial gain. But then it is criticalto prove the non-financial benefit and to define who it benefits.

"Fettering of discretion to access available assets in principle is invalid conduct for a fiduciary. A trustee is not expected to forego personal views and principles. Those views and principles should be recognised and, where she cannot exercise fair and impartial judgement owing to a conflict of beliefs, she should abstain."

Geral summarised common law cues thus:

- Determine trustees' powers refer to the fund's rules;
- Determine the best interests of the beneficiaries of the particular fund;
- "Benefit" should be measurable and regularly measured and reported on;
- Irrelevant interests are irrelevant, no matter how beneficial they are perceived to be to the "world at large"; and
- It is wrong to fetter permitted investment discretion.